

Managing China-U.S. Energy Competition in the Middle East

The bid by the China National Offshore Oil Corporation (CNOOC) to acquire Unocal earlier this year triggered not only a hostile reaction in the U.S. Congress but also growing interest and debate within the foreign policy community about the rapid growth in China's energy demand and the prospect for competition between the United States and China for access to global oil and gas resources.¹ Henry Kissinger has gone so far as to argue that competition over hydrocarbon resources will be the most likely cause for international conflict in coming years.² China's hunt for oil is clearly influencing its foreign policy toward its neighbors, such as Russia, Japan, and the Central Asian states, and toward regions as far afield as sub-Saharan Africa and Latin America.³ As China seeks access to global energy resources, its status as a rising power is already enabling it to exercise influence in ways that make it more difficult for the United States and the West to achieve their goals on a number of issues. The potentially explosive combination of a China less willing to passively accept U.S. leadership and the prospect of competition between China and other states for control over vital energy resources poses particularly critical challenges to U.S. interests in the Middle East.

Chinese engagement in the Middle East has expanded economically, politically, and strategically over the last several years. Since the late 1990s, Beijing's policies toward the region have been closely linked to the objectives of the three major, state-owned Chinese energy companies—the China National Petroleum Corporation (CNPC), the China National Petrochemical Corporation (Sinopec), and CNOOC—to seek access to Middle Eastern oil and gas, frequently on an exclusive basis. Since 2002, the Middle

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The Washington Quarterly • 29:1 pp. 187–201.

East has become the leading arena for Beijing's efforts to secure effective ownership of critical hydrocarbon resources, rather than relying solely on international markets to meet China's energy import needs. There is every reason to anticipate that China will continue and even intensify its emphasis on the Middle East as part of its energy security strategy. China will likely keep working to expand its ties to the region's energy exporters over the next several years to ensure that it is not disadvantaged relative to other foreign customers and to maximize its access to hydrocarbon resources under any foreseeable circumstances, including possible military conflict with the United States. It seems doubtful that Chinese energy companies' fledgling efforts to lock up petroleum resources will succeed in keeping a critical mass of oil reserves off an increasingly integrated and fluid global oil market. Nevertheless, China's search for oil is making it a new competitor to the United States for influence in the Middle East. If not managed prudently, this competition will generate multiple points of bilateral friction and damage U.S. strategic interests in the region.

The Middle Kingdom Meets the Middle East

China's current emphasis on the Middle East as an energy market is historically unique. Until the 1990s, Chinese foreign policy toward the region reflected other goals. In the 1960s and through most of the 1970s,⁴ Chinese policy did little more than rhetorically align Beijing with radical elements of the Arab world and posture in support of the Palestinian cause, consistent with China's support for "national liberation movements" worldwide. From the Chinese Communist Party Central Committee's historic plenum in 1978 that initiated China's domestic reform and opening to the West through the early 1990s, China engaged the Middle East more deeply, pursuing new policies to assist its modernization priorities. In particular, Beijing sought to obtain support for China's military modernization, as well as cash for economic development, by providing arms not only to both sides of the Iran-Iraq War (1980–1988) but also by cooperating with Israel in the 1980s to develop its F-10 fighter aircraft, selling Saudi Arabia CSS-2 intermediate-range ballistic missiles in 1988, and engaging in discussions with Libya and Syria about the possible sale of M-9 ballistic missiles, which Washington pressured Beijing to halt.

RIISING DEMAND

China's market-oriented economic reforms sparked exponential increases in energy demand, fueling an expanding industrial base, burgeoning commercial enterprises, and rising living standards.⁵ When anticipated petroleum

reserves in Xinjiang province and in the East and South China Seas failed to meet expectations and with the Daqing field's reserves running down, China's energy production, particularly its domestic oil production, failed to keep pace, and China became a net importer of crude oil in 1993.

Since then, the growth in China's demand for imported oil has been enormous and has had a mounting impact on global energy markets. From 1993 to 2002, Chinese oil demand grew close to 90 percent, while domestic production grew less than 15 percent. By 2004, with the economy still growing at 9.5 percent annually and as the world's third-largest automobile market, adding more than five million vehicles each year, Chinese oil demand had risen to six million barrels per day, with 40 percent coming from imports. Some 40 percent of oil demand growth worldwide over the past four years has come from China, illustrating the magnitude of China's demands on the world's oil markets.⁶ China's demand is expected to continue to grow at impressive rates for at least the next two decades, exacerbated by the country's notoriously inefficient energy use.⁷

Rising energy demand in China is prompted by a variety of factors, including industrial expansion and transportation growth. Most of China's total energy demand will continue to stem from industrial activities requiring ever more electricity. Although coal will remain the dominant fuel source for power generation in the foreseeable future, limitations on China's ability to expand its use of coal imposed by technical shortcomings, as well as infrastructure and transportation constraints, mean that the percentage of China's electrical power generated by oil- and gas-fired plants will increase in the near term. Beyond the power sector, the fastest-growing use of energy in China is for transportation, driven by an automobile market that is one of the country's foundational growth sectors. This trend will inevitably sharply raise the percentage of the country's overall energy needs that must be met through hydrocarbon fuels. China's automobile market is expected to become the world's second-largest within a decade, a development that on its own would ensure robust growth in demand for oil. China now has about 23 million cars; Sinopec executives estimate that there will be 130 million cars in the country by 2030.⁸

For Chinese leaders, these developments place a rising premium on their ability to access oil and gas resources beyond China's borders.⁹ China now purchases close to three million barrels per day of crude oil from abroad, making it the world's third-largest crude oil importer after the United States

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and Japan. The International Energy Agency (IEA), the international organization in which the world's oil-consuming nations pool information about petroleum stocks and coordinate their actions with respect to strategic petroleum reserves, predicts that China's oil demand will rise to about 10 million barrels per day by 2030, of which 80 percent will be imported.¹⁰

LET THE IMPORTS BEGIN

Because of its new need to supplement lagging domestic production with oil imports, China embarked on a new phase of energy-driven engagement with the Middle East in the 1990s. China initially established import relationships with Oman and Yemen, two of the smaller Persian Gulf states, because they produced a light, "sweet" crude that Chinese refineries could handle with relative ease.¹¹ Over the last decade, China has stepped up efforts to cultivate ties with other, smaller Gulf producers such as Kuwait and the United Arab Emirates, as well as with non-Persian Gulf energy producers in the region, such as Algeria, Egypt, Libya, and Sudan. In 1997, as part of the first round of significant overseas investments by the state-controlled Chinese energy companies, CNPC took the largest share in a multinational joint venture to explore and develop oil fields and build a pipeline to Sudan at the same time that the United States was imposing a blanket trade embargo on that country preventing U.S. energy companies from competing for these projects.¹² (This development foreshadowed the problems that have arisen more recently regarding Chinese opposition to the imposition of sanctions on Sudan over the Darfur genocide.)

These initial efforts with second-tier producers notwithstanding, by the second half of the 1990s, China was focusing its efforts to access energy resources in the Middle East on the three major oil producing states of the Persian Gulf, in ascending order of their importance to global energy markets: Iraq, Iran, and Saudi Arabia. In June 1997, a consortium of Chinese energy companies and China North Industries Corporation (NORINCO), a major industrial conglomerate that is among other things a significant arms producer and exporter, signed a 22-year production-sharing agreement with Saddam Hussein's regime to develop Iraq's second-largest oil field after the lifting of UN sanctions on the country. In the post-Saddam period, the status of China's 1997 agreement with Iraq remains uncertain, but Chinese companies can be expected to compete vigorously for upstream opportunities, i.e., the exploration and production of crude oil, in Iraq once the security and political environments permit foreign energy companies to operate there. As the Chinese companies wait for Iraq to open up, they are concentrating their efforts to access Middle Eastern energy resources, especially oil, on Iran and Saudi Arabia.

China has dramatically expanded its imports of crude oil and petroleum products from Iran since the mid-1990s, and Iran's oil minister said at the end of 2004 that Tehran expected China eventually to displace Japan as the Islamic Republic's leading market for oil exports.¹³ Since the beginning of this decade, China has also been seeking to access Iranian oil resources more directly. Iran is attractive in this regard because, in contrast to Saudi Arabia, its upstream oil sector is at least theoretically open to foreigners under the Islamic Republic's 1987 law permitting the Ministry of Petroleum and the National Iranian Oil Company (NIOC) to establish contracts with either local or foreign oil companies, establishing what has come to be described as the "buy back" system. Under this system, the contracting company typically funds all investments to develop a new or existing field and is compensated by NIOC through a share of that field's production that is supposed to be sufficient to give the company a guaranteed rate of return on its investment. Chinese companies have recently been successful in concluding a number of high-profile deals in Iran, and more deals appear to be in the offing. Overall, projected Chinese investments in oil exploration and production, petrochemicals, and natural gas infrastructure in Iran could exceed \$100 billion over the next quarter-century.¹⁴

Among all its energy relationships in the region, however, China recognizes Saudi Arabia's uniquely dominant role among the world's oil producers and continues to work hard at building closer ties to the kingdom. Beijing's efforts to develop a strategic relationship with Riyadh entered a new phase with the 1999 visit of then-Chinese president Jiang Zemin. On that trip, Chinese and Saudi leaders signed an oil cooperation agreement that, in Jiang's words, inaugurated a "strategic oil partnership" between the two countries.¹⁵ The agreement stipulated that Saudi Arabia would open its domestic oil and gas market to China except for upstream oil exploration and production. In return, China agreed to open its downstream sector (refining products from crude oil for marketing to end users) to Saudi Aramco, the Saudi national oil company. This basic bargain was positive for Beijing in both of its dimensions. China quickly expanded its imports of Saudi oil. Even though Chinese refining capability was not well suited to heavier Saudi crudes, the Saudis shifted some of their lighter crudes to the Chinese market from other customers with more developed refining infrastructures. By 2002 the kingdom had become China's leading foreign supplier of crude oil. At the same time, China has attracted much needed Saudi investments

China is now the world's third-largest crude oil importer, after the U.S. and Japan.

in joint ventures to expand and upgrade Chinese refining capacity.¹⁶ Some academicians and officials familiar with upstream oil and gas production in China also privately say that Saudi Aramco may have been a source for advanced technology and expertise that enabled Chinese energy companies to improve their production from and management of existing fields at home.¹⁷ The transfer of such technology from the United States is effectively barred under regulations governing the export of dual use and other strategically sensitive items.

No region compares to the Persian Gulf as a priority for Chinese energy planners.

Beijing paid premiums to encourage Saudi performance. Since the early years of this decade, China has allowed the Saudis to establish themselves in a very lucrative position, supplying the Chinese textile industry with petrochemical products. With Chinese cooperation, the Saudis were able to displace South Korea and other traditional Asian suppliers to

become the leading supplier to Chinese textile manufacturers. A Chinese academician familiar with the textile industry said that, dollar for dollar, the Saudis make more from their petrochemical business in China than any place else.¹⁸ In 2004, Sinopec won one of the three concessions that the Saudis awarded to foreign energy companies to develop the kingdom's nonassociated gas resources—natural gas found in geologic formations that do not also contain crude oil. The economic benefits of this arrangement to Sinopec are unclear, and the deal appears to have been to a large extent politically motivated. A consultant at Wood MacKenzie, the British energy consultancy, characterized the agreement explicitly as “a political deal. It's about forming relations with Saudi Arabia in order to secure China's long-term energy needs so when they do come looking for crude they'll be viewed favorably.”¹⁹

BEYOND ENERGY

Beijing is supporting the efforts of Chinese energy companies to win deals in the Gulf with regular high-level official visits to and from the region.²⁰ China is also following up on its expanding network of energy deals in the Gulf by becoming a more important exporter of manufactured goods and capital to the region.²¹ In Iran, for example, NORINCO is helping expand the Tehran subway systems, a Chinese fiber optic manufacturer is helping build a broadband network, and Chinese automobile and television manufacturers have opened factories. From a strategic perspective, these investments are meant to bolster China's positive image in Tehran as a long-term customer for Iranian oil and gas at a time when Iran's options for interna-

tional economic cooperation are limited by its poor political standing with the United States.

China is also expanding its export and investment ties to Saudi Arabia. In the last 10 years, the annual volume of Saudi imports from China has risen steadily, expanding roughly 600 percent in aggregate terms over the last decade.²² Chinese investment in Saudi Arabia has also expanded significantly. Strategically, these trade and investment ties are meant to reinforce Beijing's efforts to establish itself in Saudi calculations as a desirable long-term customer for the kingdom's oil exports. Chinese officials also appear to believe that, by cultivating closer ties to Saudi Arabia, a long-standing U.S. ally, they may compel the United States to take China more seriously as a global player.²³

'GOING OUT' FOR MORE

To meet its rising energy demand, in 2002, around the time that Hu Jintao became general secretary of the Communist Party, China adopted a "going out" (*zou chu qu*) policy of encouraging its three national oil companies to build up secure supplies abroad through purchasing equity shares in overseas markets, exploring and drilling abroad, constructing refineries, and building pipelines to Siberia and Central Asia.²⁴ Beyond the voracious appetite of Chinese factories and vehicles for hydrocarbons, adoption of the going-out strategy in 2002 was driven by Beijing's unease over imminent war in Iraq and uncertainty about the U.S. posture toward China, particularly in the event of armed confrontation over Taiwan.

The demands of the going-out strategy have led China inexorably toward deeper engagement with the energy-producing states of the Middle East. Chinese energy companies have concluded or are pursuing deals on every continent, but no region in the world compares to the Persian Gulf as a priority for Chinese energy planners. Chinese leaders had hoped to turn to geographically closer sources of supply in Russia and Central Asia to meet the bulk of China's oil and gas needs, but these hopes have not been realized, and Chinese confidence that Russia can be a genuine alternative to the Persian Gulf has frayed considerably. In 2003, for example, China believed that it had assured construction of a pipeline from eastern Siberia into China to join a line running south from Daqing, but by 2004 Russia appeared to be reneging on the deal because of Japanese financial incentives to move the projected pipeline's terminal north from China to Russia's Pacific coast, opposite Japan. Since then, the Russians have indicated a willingness to reconsider adding a pipeline spur to China's Daqing field, but the Chinese have found the Russian decisionmaking process on pipelines, as well as Beijing's major effort to establish a relationship with a now-defunct Yukos, frustrating

and unsettling. Although Russia still plays an important role in Beijing's plans for diversifying energy sources, China continues to look to the Middle East as a growing source of hydrocarbon imports to meet its escalating energy needs. Overall, the Middle East now provides about 60 percent of China's oil, with Iran, Oman, Sudan, and Yemen acting as important suppliers alongside Saudi Arabia. According to the IEA, by 2010 as much as 80 percent of China's oil imports could come from the Middle East.²⁵

Middle Eastern Perspectives

China's energy-driven initiatives in the Middle East have been generally well received in the region. Both Iran and Saudi Arabia have responded positively to Chinese overtures. For Iran, the political and strategic advantages of cultivating closer ties to China seem obvious. As Tehran comes under increased international pressure over its nuclear activities, the support of a permanent member both of the UN Security Council and the International Atomic Energy Agency (IAEA) Board of Governors provides much needed international political cover. Given China's history of supplying arms and sensitive military technology to Iran, Tehran almost certainly calculates that Beijing might play such a role again. Under new Iranian president Mahmoud Ahmadinejad, who seems to disdain Europe almost as much as the United States and has spoken openly about the imperative for Iran to forge strategic alliances with strong, non-Western countries such as China, the Chinese "option" is likely to become even more attractive.²⁶ Tehran sees China's support for watering down an IAEA resolution referring Iran's nuclear program to the UN Security Council and China's abstention on the final weakened resolution as an early benefit.

Just as Chinese oil companies sometimes pay market premium for access to hydrocarbon resources, Iranian officials seem willing to pay their own premiums for better relations with China. Although China is a large market, deals with Chinese oil companies currently do little to help Iran obtain the advanced exploration and production technologies needed for its own upstream sector. Western oil industry executives familiar with negotiations between Iran and foreign oil companies say that Chinese companies, in contrast to their Western counterparts, come to the bargaining table with experience and technical capabilities that, for the most part, the NIOC already has.²⁷ The oil and gas deals that Iran has concluded with China have a distinctly strategic quality to them; they seem intended to ensure access to an important export market and bolster a developing political relationship rather than to bring about the transfer of civilian technologies or infusions of capital.

In contrast to Iran, Saudi Arabia is a long-standing U.S. ally, complicating Beijing's efforts to cultivate better relations with Riyadh. The Saudi leadership, however, was disturbed by the anti-Saudi backlash in Congress and in U.S. public opinion following the September 11 attacks. Saudi leaders, including then-Crown Prince, now King, Abdullah, were also disappointed by what they perceived as President George W. Bush's less-than-vigorous public defense of the U.S.-Saudi relationship. They were also dismayed by what from their perspective were serious deficiencies in the Bush administration's Middle East policies during its first term in office.²⁸ Although the atmospherics of U.S.-Saudi relations improved somewhat with the Bush-Abdullah summit in Crawford, Texas, in April 2005, the dismay with U.S. policy continues. In September, for example, Saudi foreign minister Saud al Faisal publicly criticized U.S. policy toward Iraq for allowing the country to disintegrate toward civil war.²⁹

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As a result of these concerns, the Saudi leadership is pursuing a hedging strategy toward the United States, its traditional partner, by developing a more robust strategic relationship with China. Similar to Iran, the kingdom is paying something of a premium to encourage this relationship. For example, it is not clear that Chinese involvement in Sinopec's previously discussed 2004 agreement to develop some of the kingdom's nonassociated gas resources was, from a Saudi perspective, fully congruent with Riyadh's original goals in allowing foreign participation. Asked to comment on the agreement, a senior Saudi Aramco executive observed wryly, "Well, getting foreign companies in was always about technology transfer. And we've achieved it, from Aramco to Sinopec!"³⁰ Western oil industry executives note that, when Saudi energy minister Ali Naimi first approached Abdullah in 2003 about increasing Saudi Aramco's investment budget to expand the company's oil production capacity, at least partly in response to exhortations from Washington, he was rebuffed. It was only after the Chinese established their interest in increased Saudi production capacity that Aramco's investment budget was increased substantially.³¹

As the Saudis work to establish the basis for a future China option, they can reap some more immediate benefits. Saudis, similar to Iranians, calculate that China could expand its role as a supplier of advanced weapons and related technology. In addition to serving as a strategic hedge for Riyadh, China provides the Saudis with a safe haven for their oil wealth. After the 1997 Asian financial crisis, Saudi officials were impressed by Beijing's deter-

mination to protect the value of China's currency. After the September 11 attacks, as the United States became a less attractive destination for Saudi investments, the Saudis have turned increasingly to China to help recycle some of the enormous liquidity accumulating in the kingdom from record-high oil revenues.

Implications for Washington: Toward a Management Strategy

The Chinese drive for energy is already a source of tension in bilateral relations. China's efforts to establish influence with Middle Eastern energy producers have thwarted U.S. efforts to impose sanctions on Sudan over the Darfur genocide and are currently complicating Washington's attempts to persuade the IAEA to refer Iran to the Security Council for violating its nonproliferation obligations. Over time, China's engagement in the region could, at least theoretically, provide Iran strategic backing for a foreign policy posture that would eschew engagement with the West and challenge Western interests more assertively.

Chinese investments in Iran's oil and gas sectors are exceeding the limits set to trigger secondary sanctions under the Iran-Libya Sanctions Act (ILSA), enacted in 1996 and renewed in 2001, in part to impose U.S. sanctions on foreign companies that engage in specified economic transactions with Iran. Washington's unilateral sanctions keep U.S. companies from operating in Iran, and the implicit threat of secondary U.S. sanctions under ILSA and an informal understanding reached through high-level U.S.-European consultations late in President Bill Clinton's second term has had a restraining effect on European energy investment in Iran. Now, Chinese companies are moving to fill the vacuum, in the process complicating the Bush administration's efforts to isolate Tehran economically and pressure it for its nuclear activities. The prospect that Chinese companies would move into the development of Iran's Azadegan oil and gas fields contributed to Japan's 2004 decision to sign a \$2.5 billion deal with Tehran to develop part of these fields. The Bush administration had specifically worked with European allies to obtain assurances that European companies would not take over the project from Japan but failed to anticipate the possibility of Chinese-Iranian collaboration.

China's energy engagement in the Middle East could also conceivably weaken strategic cooperation between the United States and Saudi Arabia on a number of fronts. For one, Sino-Saudi financial coordination could have ramifications on the dollar's international standing over time. Considerable anecdotal evidence in recent years suggests that the Saudis and the Chinese have sought to draw down their dollar-denominated assets. It is

very likely that these moves were informally coordinated to ensure that neither country took a major “hit” through a sudden decline in the dollar’s value. Ultimately, Sino-Saudi collaboration could pave the way for the Organization of Petroleum Exporting Countries to decide to accept payment for oil in a basket of currencies rather than exclusively in dollars, a development that could have a significant impact on the dollar’s status as the world’s leading reserve currency.³²

It is imperative for the United States to develop a strategy for managing these challenges in the near term so that they do not escalate unduly in the medium-to-long term. It will not be possible for the United States to exclude China from the region, even if that were judged a desirable objective of U.S. policy. China will not stop its drive for energy resources in the Middle East, and Middle Eastern energy producers will not follow exhortations from Washington to cut off China. The smarter and potentially more successful U.S. policy would be to try to work with China to give it both a sense of energy security and a shared interest in a stable Middle East.

For energy security, the goal of U.S. policy should be twofold. First, Washington should initiate active cooperation with Beijing to help it implement policies and programs that would reduce China’s demand for hydrocarbons. The more that China is able to use alternative sources of energy to generate power, such as nuclear energy and “clean” coal, in which U.S. companies enjoy a technological edge, the less it will need imported petroleum. In particular, the United States should modify its export control and related policies to facilitate the transfer of nuclear technology to China. China is seeking to construct up to 40 nuclear power plants by 2020. As a result of unilateral U.S. sanctions on nuclear transfers to China from 1989 to 1998, subsequent delay in negotiating a new framework for nuclear cooperation till 2002, and continued ambiguity by Washington in response to U.S. nuclear suppliers seeking to sell to China, the United States has effectively dealt itself out of China’s nuclear market to the benefit of France, Japan, and Russia. Helping China increase its nuclear energy supply would not only provide commercial benefits to U.S. suppliers but would also decrease, at least on the margins, China’s demand for oil imports. Helping China use its abundant coal resources more efficiently through the provision of clean coal technology would also decrease the portion of the country’s petroleum imports going toward power generation and improve China’s air quality.

The Saudi leadership is pursuing a hedging strategy toward the United States.

Second, the United States should seek to persuade China to rely more on international markets and less on exclusive supply deals to meet its energy needs. Thus far, U.S. efforts to this end have consisted largely of dialogue aimed at convincing Chinese officials of the economic irrationality of paying market premiums to obtain “equity oil” deals. Unfortunately, this approach is unlikely to persuade China to rely more on global energy markets, at least

U.S. policymakers need to start thinking now about a strategy for managing the challenge.

in the near to medium term. The U.S. reaction to CNOOC’s ultimately unsuccessful Unocal bid has reinforced Beijing’s perception that China cannot rely on the equitable operation of the global energy market to meet its energy needs because U.S. policy will not allow China reliable access to that market.

A more robust U.S. approach would entail at least three diplomatic approaches beyond exhortations about market logic. First, Washington should assure China that, short of a

military conflict that the United States is not seeking, it will keep sea lanes open to China from the Persian Gulf. Next, Washington should actively encourage or at least not discourage the participation of U.S. oil companies in joint ventures with Chinese counterparts, including upstream exploration and production. Pursuing joint ventures with Chinese companies appears to be an important element of several European oil companies’ upstream strategies, but Washington’s current policy is at best ambivalent toward U.S. companies’ participation. Encouraging such participation would give China a sense of partnership with the United States in its search for energy security. Third, the United States should take the lead in encouraging and facilitating Chinese membership in the IEA. Chinese admission faces several roadblocks, chiefly the prerequisite of Organization for Economic Cooperation and Development membership and the requirement that members have a 90-day oil stockpile. China is belatedly building up a strategic petroleum reserve, aimed at providing 30 days’ supply. With China looming ever larger as a petroleum consumer and importer, if Beijing is not brought into the fold, its actions in an energy crisis could potentially disrupt the coordination efforts of the major Western nations. The United States should help the IEA and China look for creative solutions to draw China into the organization and, until Chinese membership becomes possible, to maximize coordination between the IEA and Beijing.

Beyond energy security, Washington also should engage Beijing to increase Chinese leaders’ interest in a stable Middle East. The United States certainly needs to make a compelling case to China that its relationships with Sudan and Iran not only run counter to U.S. interests but to its own by

persuading the Chinese that they have a responsibility in assuring the international objectives that it shares with the United States, including the prevention of genocide and the end of nuclear weapons proliferation. This is the goal of the senior dialogue that Deputy Secretary of State Robert Zoellick initiated with the Chinese in August 2005. To succeed, that dialogue will need to be a long-term, persistent effort in which Washington listens as well as talks. In addition, the United States needs to shape Chinese incentives and disincentives more broadly to give Beijing a clear stake in contributing actively to Middle Eastern stability. This means giving China a seat at the table by drawing it into discussions with key Middle Eastern countries and other parties about the region's future. With Iran emerging as a more powerful state and a weakened Iraq unable to play its traditional role balancing it, the United States should take the lead in developing a cooperative security mechanism for the region, along the lines of the Organization for Security and Cooperation in Europe, to go alongside historical collective security mechanisms, including bilateral alliances with key states such as Israel, Jordan, and Saudi Arabia.³³ There are many reasons for the United States to take seriously the challenge of forging a regional security framework for the Persian Gulf, if not the Middle East as a whole. Among them is the prospect that an integrated regional security structure could be useful as a forum for drawing China into a more responsible posture toward the Middle East.

Without drawing Beijing into such a posture, the Chinese drive for energy is likely to fuel a gradually escalating clash of interests between the United States and China in the Middle East. This clash of interests could threaten the attainment of U.S. goals in the region. It could also feed a more general and unwelcome antagonism between the world's only superpower and the world's fastest-growing power. An escalatory cycle of this nature is not inevitable. If it is to be avoided, however, policymakers in Washington need to start thinking now about the elements of a strategy for managing the Chinese challenge in the Middle East.

Notes

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20. On high-level Chinese visits to Saudi Arabia, see John Calabrese, "Saudi Arabia and China Extend Ties Beyond Oil," *China Brief* 5, no. 20 (September 27, 2005), http://www.jamestown.org/publications_details.php?volume_id=408&issue_id=3474&article_id=2370272.
21. See Daragahi, "China Goes Beyond Oil in Foreign Ties to Persian Gulf."
22. This calculation uses data taken from the Saudi Arabia Monetary Authority (SAMA) Web site. See <http://www.sama.gov.sa/>.
23. The authors are grateful to their Brookings Institution colleague, Jing Huang, for this point.
24. Targets of the strategy to date outside the Middle East have included Azerbaijan, Indonesia, Kazakhstan, Myanmar, Turkmenistan, and Venezuela. See Mikkal Herberg, "Asia's Energy Insecurity, China, and India," testimony before the U.S. Senate Committee on Foreign Relations, July 26, 2005.

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31. Personal communications with authors.
32. For discussion of various players' calculations regarding such a move and its likely impact, see Oystein Noreng, "Oil, the Euro, and the Dollar," *Journal of Energy and Development* 30, no. 1 (Autumn 2004): 53–80.
33. For a more complete discussion of such a regional security arrangement, see Flynt Leverett, "The Middle East: Thinking Big," *American Prospect* 16, no. 3 (March 2005): 46–47.

